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communications

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AZ CORP COMMISSION
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March 7, 2002

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

**Re: In the Matter of the Investigation of the Cost of Telecommunications
Access, Docket No. T-00000D-00-0672**

To Whom It May Concern:

With this letter, Citizens Communications submits its comments in the Commission's Access Cost Investigation, Docket No. T-00000D-00-0672. Citizens submits these comments on behalf of its three incumbent local exchange carrier affiliates operating in Arizona: (1) Frontier Citizens Utilities Rural (f/k/a Citizens Utilities Rural Company), T-01954B, (2) Frontier Communications of the White Mountains (f/k/a Citizens Telecommunications Company of the White Mountains, T-03214A and (3) Navajo Communications Company, T-02115A.

Sincerely,

Curt Huttzell
CHH

Curt Huttzell, Ph.D.
State Government Affairs

Enclosures

cc: Service List

Arizona Corporation Commission
DOCKETED

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**Citizens Communication Company's¹ Comments in Access Cost Docket
Docket No. T-00000D-00-0672**

1. *Do you believe that the Commission ought to restructure access charges? Please explain your response.*

Yes. Citizens believes that the Commission should restructure exchange access tariffs and should address both the level and structure of access rates. Specifically, Citizens recommends that the Commission bring access charges into closer correspondence with costs. The appropriate cost reference for pricing exchange access services is incremental cost, which is forward-looking, or prospective, in nature. Incremental cost may be defined as the increment (or decrement) in a firm's total cost that is caused by increasing (or decreasing) the output of an individual product or service (or group of products or services).

2. *What recommendation to the Commission would you make regarding how intrastate access charges should be reformed?*

Access charges should be brought into closer alignment with incremental costs. The relevant measure of incremental cost for this purpose is total service long-run incremental cost (TSLRIC). TSLRIC may be defined as the costs saved (or incurred) by discontinuing (or introducing) an entire product or service (or group of products or services).

Citizens proposes that TSLRIC be utilized as a cost reference for pricing access, a "measuring stick" of sorts. Citizens is NOT proposing that the Commission mandate that access charges be equal to TSLRIC. Multi-product, network firms like the Citizens' three incumbent local exchange carriers (ILECs) in Arizona are subject to economies of scale and scope. Fixing rates for all of an ILEC's products and services equal to TSLRIC would produce financial losses. Instead, Citizens is proposing that the full array of services produced by an ILEC, including access services, must contribute toward the payment of its fixed and common costs. The amount of contribution from each service should be determined by market conditions.

It is possible that revising access tariffs may reduce an ILECs' revenue streams. Citizens believes that the most appropriate means to recover the lost revenue is to increase basic local exchange rates. Citizens understands that historically the Commission has attempted to keep basic local exchange rates as low as possible. However, in the changing telecommunications marketplace, the equitable approach is to have the cost of providing service covered by the rate paid by the customer. This is

¹ Citizens Communications Company is submitting these comments on behalf of its three Arizona incumbent local exchange carrier affiliates: Frontier Citizens Rural [f/k/a Citizens Utilities Rural Company]; Frontier Communications of the White Mountains [f/k/a Citizens Telecommunications Company of the White Mountains], and Navajo Communications Company. For ease of reading, "Citizens" will be utilized throughout this document to mean both the parent company and the ILEC affiliates.

not always the case with basic local exchange rates. Therefore, it is reasonable for the Commission to allow for increases in basic local exchange service to help offset the decrease in access revenue.

Furthermore, it is clearly questionable whether Arizona ratepayers derive a benefit from low basic local exchange rates when the Arizona intrastate toll rates are so high. Intrastate toll rates include the high cost of access that interexchange carriers (IXCs) pass through to their customers. On the other hand, interstate access charges have decreased over time, putting downward pressure on interstate toll rates. Thus, there is a widening disparity between what customers have to pay when they make a call within Arizona, as compared with calls made interstate. This imbalance is not in the best interest of ratepayers.

To the extent that higher local exchange rates may threaten universal service, the Commission should look to the Arizona Universal Service Fund (AUSF) as a source for balancing any reduction in revenues that accompanies access reform. Given the amount of access revenues at stake, it may be necessary for the Commission to complete such rate rebalancing over a period of 3-5 years. Citizens contends that under no circumstances should the Incumbent Local Exchange Carriers (ILECs) be required to file rate cases as a means to make up for foregone access revenues stemming from mandatory access reform. Rate cases are complex and resource intensive, and rate case expense is passed on to customers. This procedure and its appurtenant costs are unnecessary if the Commission restructures access tariff revisions in such a way that revenue neutrality is maintained.

3. *Would you recommend the Commission address both switched and special access in an access charge reform proceeding? If your response is yes, please explain it.*

Yes. Citizens recommends that the Commission address both switched and special access in an access reform proceeding. To a certain extent, special access is a substitute for switched access; therefore, the rates charged for one form of access cannot exceed the difference in costs of obtaining the same result by substituting the other form. Moreover, access reform measures should also address establishing a rate structure that better reflects the way in which access costs vary with usage. Such a restructuring will almost necessarily introduce certain fixed elements into the switched access rate structure that resemble special access, such as charges for entrance facilities and dedicated transport.

4. *Parties who desire that switched access charges be reformed often state that switched access charges in general, and the CCL rate element in particular, contain implicit subsidies. Do you agree with this statement? Please provide an explanation of the rationale for your position, including any computations that you might have made.*

The current level of Citizens' exchange access rates in Arizona generously supports basic local exchange services and keeps basic rates low. This support may be described as an "implicit subsidy." In contrast to the notion of an implicit subsidy,

economic theory teaches that a service (or group of services) may be said to be the source of a cross subsidy if the revenues produced are greater than the service's (or services') stand alone cost ("SAC"). SAC may define as the cost a specialized firm incurs when producing a good or service. Citizens is unaware of any evidence showing that the switched access charges of Citizens' affiliated ILECs in Arizona generate revenue in excess of the SAC of exchange access. Thus, Citizens cannot conclude that exchange access is the source of a cross subsidy within its Arizona operations.

Similarly, economists teach that within a multi-product firm, a service (or group of services) may be said to receive a cross subsidy if the incremental revenues produced are less than the service's (or services') TSLRIC. Recent TSLRIC estimates of basic local exchange services for Citizens' three Arizona ILECs show these services are priced well below TSLRIC, strongly indicating they receive a cross subsidy. With regard to the Carrier Common Line (CCL) charge specifically, this is a usage-sensitive rate element designed to recoup the costs of supplying access lines. An access line is the connection between the customer's premises and the first switch in the network. Access line costs do not vary with usage. ILECs incur costs supplying access when consumers subscribe to basic local exchange service, not when subscribers place and receive telephone calls.

Economic theory teaches that usage-based charges should not be used to recover costs that do not vary with usage. In the case of exchange access, the usage-sensitive CCL charge results in access rates that are inefficiently high. IXC's are prevented from minimizing the costs of serving their customers, and as a result, telephone subscribers limit their use of long-distance services, as a cost-cutting method.

Because CCL costs are traffic-insensitive, it is illogical and inequitable to charge customers on a usage basis for this service. For these reasons, Citizens believes that CCL charges should be eliminated. Citizens recommends that this elimination process take place over the same time period that the Commission implements the rebalancing of basic local exchange rates. Eliminating the CCL should not force ILECs to suffer reductions in total revenues but should be revenue neutral.

5. Can implicit subsidies be quantified?

While the notion of implicit subsidies may have different meanings, it is reasonable to conclude that exchange access rates produce support for basic local exchange services. This support comes from the CCL rate element and the wide margins over TSLRIC embodied in existing access rates. For any particular ILEC, one way to gauge the extent of this support is to compare the sum of the TSLRICs for each individual access service at annual volumes to the sum of the annual revenues produced from each service. The difference is the amount that exchange access contributes toward the payment of the company's fixed and common costs and contributes to cover the losses produced by services priced below incremental cost.

Another way to gauge the extent of support from access services is to focus on the supported services. As suggested above, to find whether basic local exchange

services receive a cross subsidy, the revenues from such services could be compared to their TSLRIC. When basic local exchange rates are below TSLRIC, as is the case for Citizens' three Arizona ILEC affiliates, the difference represents the amount of support required from the companies' other services, including exchange access.

a. What is the appropriate cost standard to be used to determine whether access charges are free of implicit subsidies?

As explained above, TSLRIC may be used to establish whether a service (or group of services) receives a cross subsidy, and SAC may be used to determine whether a service is the source of a cross subsidy. TSLRIC may also be used to ascertain the extent of support, or contribution, provided by a service.

b. What cost standard is used to set interstate access charges? Is this cost standard appropriate for intrastate rates?

The FCC uses two different methods to set interstate access charges. For carriers subject to rate-of-return regulation, the FCC rules embodied in Part 69 establish access charges on the basis of fully distributed cost (FDC). FDC methods rely upon historical (or embedded) cost. For carriers subject to price cap regulation, the FCC has severed the relationship between access rates and FDC. The maximum rates that carriers may assess are determined annually by an index of inflation less productivity.

Citizens believes that the Commission should not prescribe intrastate access charges using FDC methods. FDC pricing standards are inherently arbitrary.

6. Do you believe that interexchange carrier switched access charges ought to exist? Please provide your rationale for your position on this matter.

Yes. Citizens believes that switched access charges should continue to be levied because they serve a useful public purpose. Supplying exchange access causes ILECs, like Citizens' three Arizona affiliates, to incur costs that should be recovered from IXCs. Assessing exchange access charges encourages IXCs to place no more demands on ILEC resources than necessary to provision long-distance services.

7. Please provide the following to assist in developing a rough estimate of the extent to which implicit subsidies exist in access charges assessed by Arizona local exchange companies.

a. What is your estimate of the implicit subsidies in access charges that exist on a statewide basis?

Citizens has not attempted to produce such an estimate.

b. Please explain how that estimate was developed.

Please see Citizens' response to Question 7(a) above.

c. What is your estimate of the existing implicit subsidies that exist by local exchange company?

Please see Citizens' response to Question 7(a) above.

8. Should access charges be set at the same rates as unbundled network elements for the same network elements and functionalities? Please explain your response.

No. Access charges should not be set at the same rates as unbundled network elements ("UNEs"). UNEs are not the same as services, even if one component of a service performs the same function as a UNE. For example, the access service called local switching shares switching costs with other functions, such as switching local and EAS calling. A local switching UNE does not share switching costs with other UNEs or network functions but accounts for all switching costs.

Even though access rate elements should not be made equal to UNE rates, differences between the rates charged for UNEs and the rates for exchange access should not exceed differences in incremental costs. Rate differentials that are larger than differences in cost will only provide incentives for tariff shopping and arbitrage, which clearly does not serve the public interest.

9. Your responses to the following questions will assist the Commission in determining how to proceed with this case from a procedural perspective.

a. What procedure would you recommend be used to address switched access charge reform? For example, would you recommend a generic proceeding to address the issues in general with the objective being the reform, restructure and resetting of switched access charges for every LEC in the State?

Citizens recommends that the Commission institute a generic proceeding or rulemaking to address access reform issues in general.

b. What issues do you believe should be addressed in a proceeding to determine whether and to what extent intrastate access charges ought to be reformed?

Citizens recommends that a generic proceeding or rulemaking involving access reform should address the following issues:

- The appropriate level and structure of access rates;
- The extent to which basic local exchange services should be supported by exchange access services;

- Whether and to what extent basic local exchange rates should rise in response to reducing contributions from access rate elements, and
- Whether and to what extent support from the AUSF should replace lost access revenues.

c. Would you recommend that the Commission limit the initial switched access charge proceeding to the largest ILECs in Arizona? If your response is yes, please identify those companies that you believe should be included in this proceeding.

No.

d. Would you recommend that the Commission address access charge reform for large, intermediate and small local exchange companies (as defined in the Commission's Arizona Universal Service Fund rules) individually? Please explain.

No. All carriers should have the same access rate structure, if not the same level.

e. Would you recommend that the proceeding address switched access charges assessed by CLECs and/or other telecommunications companies?

Yes.

f. Given your vision of what the proceeding would address, how much time do you expect would be required to complete the proceeding?

Citizens anticipates that Commission Staff would hold workshops and gather data. Citizens estimates that once Staff begins those processes, it will take about a year to present a final proposal to the Commission.

10. For companies that provide access service, please provide the dollar amount of revenues from switched access charges that you received by rate element, by month, for the period July 1, 2000 through June 30, 2001.

It is Citizens' position that the information requested is proprietary information. Because Citizens understands the Commission's interest in this information, the company will work with Commission Staff to execute a confidentiality agreement to protect the proprietary information.

11. For companies that purchase access service, please provide the dollar amount of the payments for switched access charges that you made (by company, rate element, and month if possible) for the period July 1, 2000 through June 30, 2001.

Not applicable.

- 12. Do you believe that it would be possible to eliminate the potential that local exchange service providers can exert monopoly power in the access service market by assessing the switching, transport and CCL charges on the end users rather than on the interexchange carriers? Could customers then shop for local exchange service customers for the least cost provider of access in addition to local service, etc.?**

No. Monopoly power may be defined as the ability to control price and exclude competitors. To the extent an ILEC may possess monopoly power, the sources of this power are not stemmed by having the ILEC levy exchange access charges against retail customers instead of IXCs. To the contrary, in a completely deregulated market for exchange access, any monopoly power possessed by ILECs would be partly, if not wholly, offset by the monopoly power exercised by the dominant IXCs.

- 13. Do you believe that there is a difference in the costs of providing interstate-switched access versus intrastate-switched access service? In your response, please include a description of how costs are defined in your response and how those costs relate to costs allocated to the intrastate jurisdiction under the FCC's Separations rules.**

No. There is no difference between the costs of supplying interstate and intrastate-switched access when costs are defined as incremental. In contrast, the FCC's Separations rules assign embedded costs between the state and interstate jurisdictions using FDC methods. While some method is necessary to determine how much of a company's revenue requirement should be recovered from each jurisdiction, FDC methods should not be used to fix maximum, minimum or precise rates.

- 14. In the CALLS Decision, the FCC implemented changes that would eliminate carrier common line charges and establish an interstate universal service support mechanism. Do you believe that the Commission ought to address the Arizona Universal Service Fund mechanism concurrent with the reform of intrastate access charges?**

Yes. It is imperative that the Commission address AUSF reform simultaneously with restructuring access charges, and Citizens strongly recommends that the Commission consolidate the AUSF docket and this docket. In the alternative, the two dockets should proceed concurrently. At the very least, the Commission must recognize that the issues raised in the two dockets are inextricably intertwined. Citizens respectfully reminds the Commission of its November 1, 2001 comments in Docket No. RT-00000H-97-0137:

...In the high-cost, rural areas of Arizona, preserving and extending universal service has depended upon support from toll and access rates, particularly access rates.

However, the support provided by toll and access is no longer sustainable in the presence of competition and changing federal regulatory policies. Equal access has already driven intraLATA toll rates closer to cost and substantially lessened their contribution to the affordability of basic service. Federal regulatory policy continues to reduce interstate access charges and widen the disparity between intrastate and interstate rates, setting up even more powerful incentives for interexchange carriers to misreport the jurisdictional nature of long-distance traffic. In short, competition and conflicting regulatory policies have already reduced the amount of support provided by toll rates and seriously threaten the adequacy of support from exchange access charges...

Moving toward greater explicit support from the AUSF would contribute significantly toward the preservation of universal service in rural Arizona. Unless reliance upon access charges as a means of promoting universal service is lessened, widely available basic local exchange service at affordable rates is seriously threatened in high-cost, rural areas. Basic local exchange rates may have to rise significantly above current levels to replace traditional sources of support, or rural carriers, such as Citizens' three Arizona affiliates, may not be able to generate the funds necessary to maintain, improve, and expand their local operations. Greater AUSF support is a fair and effective explicit replacement for the current system of implicit support.

15. The FCC released its Access Charge Reform Order ("MAG Order") for rate of return companies on November 8, 2001. Please comment on the extent to which you believe the ACC should adopt any components of the MAG Order.

In its MAG Order, the FCC took three steps affecting rate-of-return carriers that Citizens recommends this Commission follow in Arizona. First, the FCC removed the CCL charge from the interstate access charge rate structure. In doing so, the FCC found the CCL charge to be an inefficient cost recovery mechanism and concluded removing it would move switched access rates toward lower, cost-based levels.²

Second, the FCC's MAG Order increased the ceilings it had placed on Subscriber Line Charges ("SLCs") for residential and single-line business local exchange services. SLCs are flat monthly fees assessed on access lines and intended to recover common line (*i.e.*, access line) costs. Increasing SLCs has the same effect on subscribers as increasing basic local exchange rates. When ordering this second step,

² MAG Order at ¶¶ 15 and 40-41.

the FCC repeated its earlier conclusion that common line costs should be recovered on a flat-rated instead of a per-minute basis because these costs do not vary with usage.³

Third, the FCC substituted a new universal service support mechanism to replace the implicit support lost by eliminating CCL charges. It is called the Interstate Common Line Support mechanism and is intended to make up for the difference between the carriers' common line (*i.e.*, access line) costs and the revenue produced by SLC charges.⁴ This Commission should take similar steps in Arizona. To the extent that removing CCL rates from intrastate access tariffs reduces carriers' revenues, the reduction should first be made up from local rate increases and secondarily from the AUSF.

16. Should the Commission address CLEC access charges as part of this Docket?

Yes.

17. Should additional considerations be taken into account when restructuring and/or setting access charges for small rural carriers? Please explain your response.

Please see Citizens' response to Question 14 above.

18. What is the effect of Qwest's Price Cap Plan on the issues raised in this proceeding as they pertain to Qwest? With regard to Qwest, switched access is a Basket 2 service and special access is a Basket 3 service. What impact does this have, if any, on restructuring access charges in this proceeding, as it would pertain to Qwest?

Citizens does not have a comment on this issue at this time.

19. With regard to Qwest, what impact would Qwest receiving Section 271 authority have on the issues raised in this proceeding? Please explain your response.

Citizens does not have a comment on this issue at this time.

20. One of the stated objectives of the Qwest Price Cap Plan was to achieve parity between interstate and intrastate access charges. Is this something that should be looked at by the Commission in this proceeding?

Yes. Matching the federal access rate structure and moving toward the federal access rate level would result in bringing state access charges into closer alignment with incremental costs. As explained in response to Question 2 above, ILECs should not have to file rate cases to recover any reduction in total revenue as a result of moving

³ MAG Order at ¶¶ 15 and 42-43.

⁴ MAG Order at ¶¶ 15 and 128.

toward the level and structure of interstate access rates. Revenue reductions should first be made up from rebalancing basic local exchange rates and then from the AUSF.

21. Are there other issues besides the rate restructuring and costing issues raised herein that should be addressed by the Commission in this Docket?

Yes. Please see Citizens' response to Question 14 above.

22. Are there other State proceedings and/or decisions that you would recommend the Commission examine before it proceeds with this Docket? Please attach any relevant State commission decisions to your comments.

Yes. The Commission should examine the issues raised by the parties that filed comments in its AUSF Reform Proceeding, Docket No. RT-00000H-97-0137.

23. Please provide your recommendations for a procedural schedule in this case.

Citizens recommends that the Commission hold workshops with all interested parties and allow the interested parties the opportunity to provide written responses to any proposals that are a result of those workshops. Citizens respectfully requests that interested parties be given sufficient time to prepare written comments, particularly because at Citizens, there are several levels of review before a document is submitted to the Commission. Because of the importance of this issue, a minimum of a 30-day period for written comments would be reasonable.

As noted previously, Citizens believes that the AUSF reform issue should be analyzed in the context of access reform. Consolidation of those two dockets would insure that the final decisions in both areas were consistent and in the best interest of the public.

Because this is an important issue, Citizens urges the Commission to set a procedural schedule that will allow for the necessary dialogue between parties and full briefing of legal issues. This is not a matter that should be rushed to a final decision, but instead should be fully analyzed and discussed, so a thoughtful and prudent final determination can be made.

With the foregoing recommendations in mind, Citizens proposes the following procedural schedule leading up to a final recommendation from the Staff:

- **4/12/02:** The Staff holds a Workshop to address:
 - The nature and scope of the proceeding, including:
 - Whether it should become a rulemaking or remain a generic investigation,
 - Whether it should be consolidated with the AUSF docket;

- Whether the access services under consideration should include CLECS and both large and small ILECs;
- Identification of the issues, given the nature and scope of the proceeding;
- The relevant data and information that must be collected and the manner of collection, and
- A procedural schedule.
- **5/17/02:** Written comments of the parties submitted on the matters discussed at the 4/12/02 Workshop.
- **8/15/02:** The Staff submits a proposed rule or policy statement based on its investigation.
- **10/17/02:** Written comments of the parties submitted on the Staff's proposed rule or policy statement.
- **11/15/02:** The Staff conducts a workshop addressing its proposed rule or policy statement.
- **2/14/02:** The Staff submits its proposed rule or recommended decision to the Commission.

24. Please comment on the issues raised in Docket No. T-01051B-01-0391, In the Matter of Qwest Corporation's Tariff Filing to Introduce a New Rate Structure for an Access Service Used by Interexchange Carriers and their relationship to this Docket.

Qwest has withdrawn the tariff it proposed in the foregoing docket; therefore, the issues raised there are moot for the time being. Should Qwest file another access tariff that raises the same or similar issues, Citizens will comment at that time.

25. Please comment on any other issues you believe may be relevant to the Commission's examination of intrastate access charges.

Citizens has no further comments at this time.